Supreme Court, U.S.
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No.

In the Supreme Court of the United States

OCTOBER TERM, 1998

UNITED STATES OF AMERICA, PETITIONER

v.

LEVI STRAUSS & COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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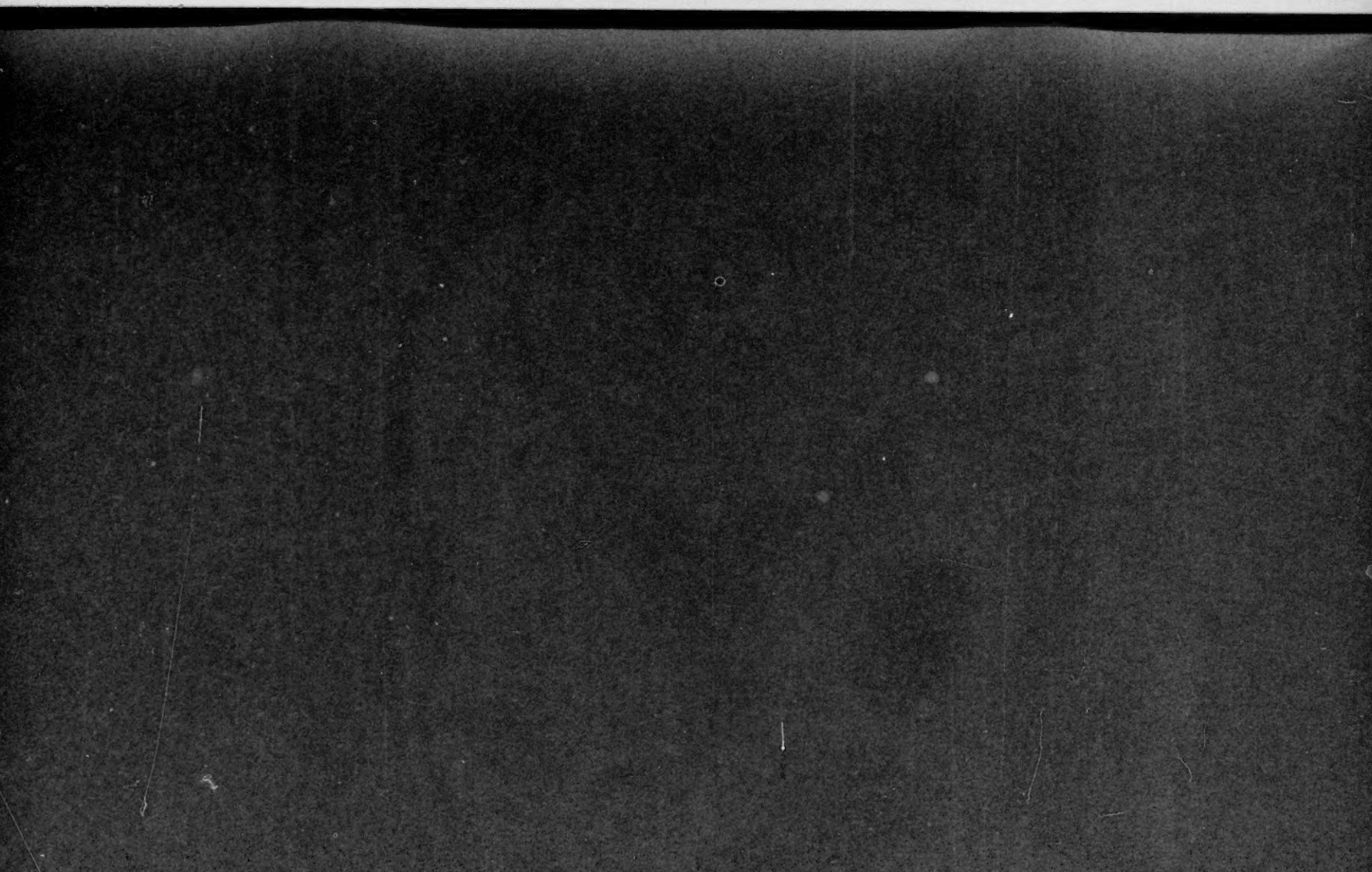

QUESTIONS PRESENTED

1. Whether regulations issued by the Treasury Department under the Tariff Act are entitled to deference in determining the proper tariff classification of imported goods.

2. Whether 19 C.F.R. 10.16(c) reasonably interprets the statutory phrase "operations incidental to the assembly process" in Subheading 9802.00.80 of the Harmonized Tariff Schedule of the United States.

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PETITION FOR A WRIT OF CERTIORARI

The Solicitor General, on behalf of the United States, respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Federal Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-13a) is reported at 156 F.3d 1345. The opinion of the Court of International Trade (App., *infra*, 14a-28a) is reported at 969 F. Supp. 75.

JURISDICTION

The judgment of the court of appeals (App., *infra*, 29a) was entered on September 22, 1998. A petition for rehearing was denied on November 24, 1998 (App.,

infra, 30a). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

1. 28 U.S.C. 2643(b) provides:

> If the Court of International Trade is unable to determine the correct decision on the basis of the evidence presented in any civil action, the court may order a retrial or rehearing for all purposes, or may order such further administrative or adjudicative procedures as the court considers necessary to enable it to reach the correct decision.

2. Subheading 9802.00.80 of the Harmonized Tariff Schedule of the United States, 19 U.S.C. 1202, provides that, with respect to:

> Articles * * * assembled abroad in whole or in part of fabricated components, the product of the United States, which (a) were exported in condition ready for assembly without further fabrication, (b) have not lost their physical identity in such articles by change in form, shape or otherwise, and (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process such as cleaning, lubricating and painting[, the duty that is to be paid is to be calculated] upon the full value of the imported article, less the cost or value of such products of the United States .

3. 19 C.F.R. 10.16(c) provides:

> Any significant process, operation, or treatment other than assembly whose primary purpose is the fabrication, completion, physical or chemical im-

provement of a component, or which is not related to the assembly process, whether or not it effects a substantial transformation of the article, shall not be regarded as incidental to the assembly and shall preclude the application of the exemption to such article. The following are examples of operations not considered incidental to the assembly as provided under subheading 9802.00.80, Harmonized Tariff Schedule of the United States (19 U.S.C. 1202):

(1) Melting of exported ingots and pouring of the metal into molds to produce cast metal parts;

(2) Cutting of garment parts according to pattern from exported material;

(3) Painting primarily intended to enhance the appearance of an article or to impart distinctive features or characteristics;

(4) Chemical treatment of components or assembled articles to impart new characteristics, such as showerproofing, permapressing, sanforizing, dying or bleaching of textiles;

(5) Machining, polishing, burnishing, peening, plating (other than plating incidental to the assembly), embossing, pressing, stamping, extruding, drawing, annealing, tempering, case hardening, and any other operation, treatment or process which imparts significant new characteristics or qualities to the article affected.

STATEMENT

1. Respondent Levi Strauss & Company brought this suit in the United States Court of International Trade to recover duties paid under protest for the importations of certain denim jeans in 1993. The garments were assembled in Guatemala from components made in the United States. App., *infra*, 14a-15a. After assembly, the garments were subjected to a "stonewashing" operation in which they were treated with a chemical enzyme to impart a faded and artificially worn appearance that was desirable to consumers. *Id.* at 2a-3a.

Under Subheading 9802.00.80 of the Harmonized Tariff Schedule of the United States, 19 U.S.C. 1202, an importer is entitled to a partial duty allowance for:

> Articles * * * assembled abroad in whole or in part of fabricated components, the product of the United States, which * * * (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process such as cleaning, lubricating, and painting.

Pursuant to authority conferred on the Secretary of the Treasury "to issue rules and regulations governing the admission of articles under the provisions of the schedules" (Tariff Schedules of the United States, General Headnote 11, 19 U.S.C. 1202 (1982)), the Treasury has specified by regulation that "[a]ny significant process, operation, or treatment other than assembly whose primary purpose is the * * * physical or chemical improvement of a component * * * shall not be regarded as incidental to the assembly" and therefore does not qualify for this duty exemption. 19 C.F.R. 10.16(c). Applying this standard, the regulations

specify that this duty exemption is not available for the "[c]hemical treatment of components or assembled articles to impart new characteristics, such as shower-proofing, permapressing, sanforizing, dying or bleaching of textiles." 19 C.F.R. 10.16(c)(4). The Customs Service determined that the "stonewashing" conducted by respondent falls within the scope of the exclusions described in the regulation and therefore denied respondent's request for a duty exemption. App., *infra*, 14a-15a.

2. The Court of International Trade has exclusive jurisdiction to review protests from Customs Service determinations. 28 U.S.C. 1581(a). The court rejected the Customs Service determination in this case and directed that the duties be refunded to respondent. App., *infra*, 14a-28a.

Relying on the decision of the Federal Circuit in *Rollerblade, Inc.* v. *United States*, 112 F.3d 481, 484 (1997), the court held that no deference was owed to the Treasury's interpretations of the classification provisions of the Tariff. The court stated that its statutory responsibility "to determine the correct decision" (28 U.S.C. 2643(b)) precludes any deference to the agency's interpretive regulations "under the administrative deference standard promulgated in *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 * * * (1984)." App., *infra*, 16a n.2.

Having thus elected to ignore the agency's regulations, the court proceeded to apply a set of judicially created factors to determine *de novo* whether Levi's stonewashing operation is "incidental to the assembly process" and therefore within the scope of the duty exception provided in Subheading 9802.00.80 of the Harmonized Tariff. As a source for such judicially-created factors, the court looked to the decision of the

Federal Circuit in *United States* v. *Mast Industries, Inc.*, 668 F.2d 501, 506 & n.7 (1981). In *Mast*, the court of appeals held that, in determining whether a process is incidental to assembly for purposes of the tariff exemption, courts should consider (i) whether the cost and time required by the ostensibly "incidental" operation may be considered minor compared to the cost and time required for assembly of the whole article; (ii) whether the operation is necessary to the assembly process; (iii) whether the operation is so related to assembly that it was logically performed during assembly; and (iv) whether economic or other practical considerations dictate that the operations be performed concurrently with assembly. *Ibid.* See also *General Motors Corp.* v. *United States*, 976 F.2d 716 (Fed. Cir. 1992). The trial court found that Levi's stonewashing process "is not necessary to the assembly process" (App., *infra*, 23a) but, relying on its recent decision in *Haggar Apparel Co.* v. *United States*, 938 F. Supp. 868 (Ct. Int'l Trade 1996), aff'd, 127 F.3d 1460 (Fed. Cir. 1997), cert. granted, 119 S. Ct. 30 (1998) (No. 97-2044 (argued Jan. 11, 1999)), the court held that the stonewashing procedure should be regarded as "incidental to the assembly process" because "numerous economic and practical reasons" require the procedure to occur concurrently with assembly and because stonewashing is "analogous to cleaning and painting which the statute specifically lists as being minor and incidental to the assembly processes" (App., *infra*, 25a, 27a).

3. The Federal Circuit has exclusive jurisdiction to review the final decisions of the Court of International Trade. 28 U.S.C. 1295(a)(5). On appeal from the decision in this case, the Federal Circuit affirmed (App., *infra*, 1a-13a).

The court of appeals held that the Court of International Trade had properly ignored the agency's regulations and had correctly applied the *Mast* factors in determining that the stonewashing of the Levi pants was "incidental to assembly" and therefore within the customs exemption (App., *infra*, 8a). On the question of the proper deference owed to the agency's regulations, the court simply cited its recent decision in *Haggar Apparel Co.* v. *United States*, 127 F.3d at 1462, and stated that it was "bound by precedent squarely rejecting the government's assertion of deference to Customs's regulatory interpretations of tariff classifications" (App., *infra*, 7a).

4. The United States filed a petition for rehearing with a suggestion of rehearing en banc. We requested the court of appeals to defer consideration of that petition pending disposition by this Court of *United States* v. *Haggar Apparel Co.*, No. 97-2044, in which this Court granted the government's petition for a writ of certiorari on September 29, 1998. On November 24, 1998, however, while the *Haggar* case was being briefed in this Court, the court of appeals denied the rehearing petition in the present case. App., *infra*, 29a-30a.

REASONS FOR GRANTING THE PETITION

This case presents the same question of the proper deference owed to Treasury interpretations of the Tariff Act that is currently pending for decision by this Court in *United States* v. *Haggar Apparel Co.*, No. 97-2044 (argued Jan. 11, 1999). Moreover, both cases present that question in the context of the Treasury regulation (19 C.F.R. 10.16(c)) that interprets the duty allowance for operations "incidental to the assembly process" under Subheading 9802.00.80 of the Harmonized Tariff Schedule.

The petition for a writ of certiorari in *Haggar* was granted on the day before the decision in the present case was issued by the Federal Circuit. The disposition of the present case will be governed by the decision of this Court in *Haggar*. The Court should therefore hold the present petition and dispose of it in light of the decision in *Haggar*.

CONCLUSION

The petition for a writ of certiorari should be held and disposed of as appropriate in light of the Court's disposition of *United States* v. *Haggar Apparel Co.*, No. 97-2044.

Respectfully submitted.

SETH P. WAXMAN
Solicitor General

FEBRUARY 1999

APPENDIX A

UNITED STATES COURT OF APPEALS
FEDERAL CIRCUIT

No. 97-1536

LEVI STRAUSS & COMPANY, PLAINTIFF-APPELLEE

v.

UNITED STATES, DEFENDANT-APPELLANT

[September 22, 1998]
Rehearing Denied Nov. 24, 1998

Before: NEWMAN, Circuit Judge, SKELTON, *Senior* Circuit Judge, and MICHEL, Circuit Judge.

MICHEL, Circuit Judge.

The United States appeals from the judgment of the United States Court of International Trade reversing the denial by the United States Customs Service ("Customs") of Levi Strauss & Company's ("Levi's") protest that Levi was improperly denied a deduction from its duty assessment for the cost of certain fabric components manufactured in the United States. *See Levi Strauss & Co. v. United States*, 969 F. Supp. 75 No. 93-11-00726, slip op. 97-79 (Ct. Int'l Trade 1997). This case was submitted for our decision following oral argument on August 5, 1998. Because, in accordance with our case law, the Court of International Trade properly reviewed Customs's interpretation of the pertinent clas-

sification regulations without deference and because the Court of International Trade's determination that the non-assembly operations performed outside of the United States were incidental to the assembly process was not clearly erroneous, we affirm.

BACKGROUND

The merchandise at issue in this appeal consists of boys' "stonewashed" jeans sold by Levi in the United States under the Levi trademark. The jeans are assembled in Guatemala from denim fabric components and other incidental components, all of which are manufactured in the United States.

Denim fabric is composed of two types of cotton yarn woven in a crisscross pattern. One type, the weft yarn, is undyed, while the other type, the warp yarn, is dyed in indigo. However, because indigo has only a weak affinity for cotton, the indigo dye is merely painted on the warp yarn and is readily removed through washing as well as normal wear and tear. Thus, as a result of one half of the yarn being undyed and the other half having readily removable dye, the jeans fade in color fairly rapidly. As the parties here agree, this faded appearance is considered desirable to consumers. Accordingly, manufacturers, including Levi, remove the oils and waxes used in the weaving process that otherwise slow down the fading. In addition, manufacturers lighten the color by washing the jeans. These processes also soften the jeans, which it is agreed is also desirable to consumers. Some manufacturers also accelerate the washing process by stonewashing. This is where stones, or other such particles, are added to the wash to produce abrasion and thereby accelerate the wear and tear. Certain manufacturers, including Levi in the instant case, achieve the same stonewashing effect by

adding an enzyme having the brand name "Cellulase" or "Denimax" to the wash.

The denim fabric for the merchandise at issue is cut to shape in Spartanburg, South Carolina, and then shipped, along with other components, such as buttons, threads, and zippers, to Koramsa, S.A., a company located in Guatemala. Prior to May 1993, Koramsa assembled the jeans and then returned them to the United States where Levi then applied the stonewashing process. After May 1993, Koramsa also provided stonewashing in Guatemala.

Upon importation into the United States, the subject merchandise was classified by Customs as boys' one hundred percent cotton woven trousers under subheading 6203.42.40 of the Harmonized Tariff Schedule of the United States ("HTSUS"). This classification carried a duty of 17.7%. Levi filed a timely protest asserting that the cost or value of the denim fabric components manufactured in the United States should have been deducted from the duty assessment pursuant to HTSUS subheading 9802.00.80. Subheading 9802.00.80 provides a partial duty exemption for:

> [a]rticles, except goods of heading 9802.00.90, assembled abroad in whole or in part of fabricated components, the product of the United States, which (a) were exported in condition ready for assembly without further fabrication, (b) have not lost their physical identity in such articles by change in form, shape or otherwise, and (c) *have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process such as cleaning, lubricating and painting.*

(emphasis added). Customs denied Levi's protest on the grounds that the stonewashing process undertaken in Guatemala was not an operation "incidental to the assembly process" as contemplated by subheading 9802.00.80.

Levi appealed the decision to the Court of International Trade, which held that Customs incorrectly denied Levi a partial duty exemption for its denim fabric components. The Court of International Trade initially noted that subheading 9802.00.80 originated from item 870.00 of the former Tariff Schedule of the United States. Item 870.00 was amended in 1965 to the currently applicable language and the accompanying House Report stated:

> The amended item 807.00 would specifically permit the U.S. component to be advanced or improved "by operations incidental to the assembly process such as cleaning, lubricating, and painting." It is common practice in assembling mechanical components to perform certain incidental operations which cannot always be provided for in advance . . . . Such operations, if only of a minor nature incidental to the assembly process, whether done before, during, or after assembly, would be permitted even though they result in an advance in value of the U.S. components in the article assembled abroad.

H.R. Rep. No. 88-1728, at 46 (1964). The Court of International Trade explained that in *United States v. Mast Industries, Inc.*, 69 C.C.P.A. 47, 668 F.2d 501 (C.C.P.A. 1981), the United States Court of Customs and Patent Appeals, this court's predecessor court, interpreted this provision and its legislative history to provide a set of factors to be used in ascertaining whether a process is

incidental to assembly. These so-called *Mast* factors are:

> (1) Whether the cost of the operation relative to the cost of the affected component and the time required by the operation relative to the time required for assembly of the whole article were such that the operation may be considered "minor."
> . . .
> (2) Whether the operations in question were necessary to the assembly process . . .
> (3) Whether the operations were so related to assembly that they were logically performed during assembly. . . .
> (4) [W]hether economic or other practical considerations dictate that the operations be performed concurrently with assembly.

Id. at 506 & n.7.

The Court of International Trade then analyzed Levi's claimed exemption in accordance with these factors. It initially determined that, under the first factor, the relative cost of 27% of total component cost and relative time of 1.1% of total assembly time indicated that the stonewashing process was incidental to the assembly process. *See Levi*, 969 F. Supp at 79-80. However, the court concluded that the second factor weighed against granting the partial duty exemption because the stonewashing process was not necessary to the assembly process, but rather could have been conducted at other facilities, as was the case prior to May 1993. *See id.* at 79-80. The court reasoned that the third factor weighed in favor of granting the partial duty exemption because it would be logical to perform the stonewashing "at the situs of the assembly process where all other assembly and post-assembly steps are

performed and where the trained personnel are located." *Id.* at 80. With regard to the fourth factor, the court determined that economic and practical considerations weighed in favor of granting the partial duty exemption, including Levi being able to detect and correct sewing and laundry defects more easily after assembly, producing more "first-quality" garments, reducing the time to get the garments to the buyer, and saving on labor costs because there would be no need to unpack and repackage the garments. *See id.* at 80. Examining additional arguments, the court then rejected Customs's contention that permitting Levi this exemption would harm United States domestic industry. The court explained that it could find no support for the claim that the legislative intent of subheading 9802.00.80 was to protect domestic industry from domestic companies moving abroad, but rather found that it was enacted to allow, as here, domestically manufactured goods to compete with foreign-made goods. *See id.* at 80-81. Finally, the court found that the stonewashing process was analogous to cleaning and painting, which subheading 9802.00.80 specifically lists as minor, and comparable to "the curing operation which imparted crease retention and seam and surface flatness to men's pants" that was found minor and incidental in *Haggar Apparel Co. v. United States*, 938 F. Supp. 868 (Ct. Int'l Trade 1996), *aff'd*, 127 F.3d 1460 (Fed. Cir. 1997), *petition for cert. filed*, 67 U.S.L.W. 3001 (June 18, 1998). *Levi*, 969 F. Supp. at 81. Thus, the court concluded that the *Mast* factors, as well as other considerations, weighed in favor of granting Levi the partial duty exemption.

ANALYSIS

I.

The government's initial and seemingly primary argument on appeal is that the Court of International Trade erred by failing to accord deference to the interpretation by Customs of the applicable HTSUS provisions pursuant to *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 104 S. Ct. 2778, 81 L. Ed. 2d 694 (1984). In support of this argument the government points to the authority granted to Customs by 19 U.S.C. § 1500(b) (1994) to "fix the classification and rate of duty applicable to such merchandise." Moreover, it further points to Customs's promulgation, under these and other authorities, of 19 C.F.R. § 10.16(c)(4) (1998), which provides, in relevant part, that "[t]he following are examples of operations not considered incidental to the assembly as provided under subheading 9802.00.00[:] . . . (4) Chemical treatment of components or assembled articles to impart new characteristics, such as . . . dying or bleaching of textiles."

We are somewhat perplexed as to why the government has chosen to appeal this issue because we are bound by precedent squarely rejecting the government's assertion of deference to Customs's regulatory interpretations of tariff classifications.[1] *See Haggar*,

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[1] The government noted in its brief that, at the time of filing, it was considering whether to seek *in banc* review of *Haggar* or file a petition for a writ of certiorari and, therefore, "[i]n order to preserve our deference arguments, they must also be set forth in this case." Br. for Def.-App. at 25 n.16. We fail to comprehend how the government's arguments were in any sense "preserved" by making them here.

127 F.3d at 1462 ("[T]he [Court of International Trade] properly rejected the United States' argument that Customs' regulations interpreting and applying this statute are entitled to deference under *Chevron*."); *Rollerblade, Inc. v. United States*, 112 F.3d 481, 484 (Fed. Cir. 1997) ("[N]o *Chevron* deference applies to classification decisions by Customs."); *Universal Elecs. Inc. v. United States*, 112 F.3d 488, 491 (Fed. Cir. 1997) ("[N]either this court nor the Court of International Trade defers to Customs' interpretation of a tariff heading on the basis of special deference pursuant to *Chevron*."). As we have explained, "the Court of International Trade's statutory mandate to find the correct result is logically incompatible with *Chevron* deference." *Rollerblade*, 112 F.3d at 484. *See generally* 28 U.S.C. § 2643(b) (1994) (charging the Court of International Trade with the duty "to reach the correct decision"). Thus, in accordance with our prior precedent, we reiterate that no *Chevron* deference is due to Customs's interpretations of the tariff statutes and we therefore hold that the Court of International Trade's review of Customs's determinations complied with that court's statutory mandate.

II.

The government's second argument on appeal is that the Court of International Trade misapplied the *Mast* factors and that the stonewashing here was not minor and incidental to the assembly process. We find no error of law in the court's application of the *Mast* factors and we conclude that the court's determination that the stonewashing was incidental to the assembly operation was not clearly erroneous. *See Universal Elecs.*, 112 F.3d at 493 ("[o]n appeal we review the Court of International Trade's factual findings—not

those of Customs unless they coincide—for clear error. On questions of law, we defer to neither Customs' nor the Court of International Trade's interpretations; we decide such questions afresh." (Citation omitted)).

(i) The relative cost and time comparisons

The government contends that the Court of International Trade's cost comparison was inconsistent with *General Motors Corp. v. United States*, 976 F.2d 716, 11 Fed. Cir. (T) 1 (Fed. Cir. 1992) ("*GM*"). In *GM* we reversed the Court of International Trade's grant of a partial duty exemption on various sheet metal components to a U.S. automobile manufacturer. After being assembled into vehicles abroad, the vehicle bodies were subject to a finish painting process. *See id.* at 718, 11 Fed. Cir. (T) at 1-2. Central to our reversal was the Court of International Trade's failure to include in its cost analysis all paint shop operations, which included, not just topcoat painting, but also zinc phosphate spraying, submerging in an electro deposition primer tank, baking, sanding, sealant treating, applying surface primer, curing, and waxing. *See id.* at 718-20, 11 Fed. Cir. (T) at 2-5. There was no such error in the Court of International Trade's analysis here. With regard to operating costs, the Court of International Trade expressly took note of *GM* and in calculating the "wash cost" took account of all components that were stonewashed. It was not error for the court to exclude certain post-wash costs, such as packing and shipping, from its "wash cost" calculation because these costs, unlike the included costs in *GM*, were entirely separate from the stonewash operation.

We similarly conclude that there was no clear error in the Court of International Trade's comparison of capital costs. Subheading 9802.00.80 lists "washing" as

an incidental operation. Thus, capital investment in washing machines would not appear to be outside of the subheading's ambit. In addition, unlike *GM*, the Court of International Trade appears to have taken proper account of depreciation costs.

With regard to the time comparison, the Court of International Trade found that the stonewashing process accounted for 1.1% of the total time, based upon a single pair of denim jeans taking nineteen minutes to assemble and 296 pairs of jeans taking ninety-nine minutes to wash. Although the government argues that the Court of International Trade failed to take labor time into account, we are not persuaded that the time spent loading and unloading the jeans from the washing machines was anything other than *de minimis* and thus would not impact the calculation in a significant manner. We are also unpersuaded by the government's argument that the Court of International Trade should not have divided the ninety-nine minute washing time by the 296 jeans, but rather should have regarded the washing time as ninety-nine minutes per pair. This argument ignores the reality that all 296 pairs of jeans were washed together and, indeed, had to be washed together if the abrasive process was to be successful. Thus, the Court of International Trade's time comparison was not clearly erroneous.

(ii) The logic of performing the operations during assembly

The government argues that the stonewashing was not logically performed during the assembly process because it involved a different process (washing, rather than sewing) and different machinery (washing machines, rather than sewing machines). However, the government's argument appears to misconstrue this

Mast factor. The appropriate inquiry is not whether the operation is somehow identical or nearly identical to assembly itself, but rather whether the relationship between the operation and assembly is such that force of logic suggests that the operation be performed as an incident to assembly. Here, there was substantial evidence that the relationship between the stonewashing and the assembly of the jeans logically dictated that they be performed together. Thus, for example, certain paper tags and brand labels cannot be attached to the jeans prior to the stonewash because they would be mutilated by the stonewashing process. Accordingly, stonewashing the jeans at the point of assembly obviates the need to have a separate assembly staff elsewhere to attach these tags and labels. Moreover, it further obviates the need to pack the jeans for shipping only to have to unpack them elsewhere for stonewashing and attachment of tags and labels. Therefore, we conclude that the Court of International Trade's determination that this *Mast* factor weighed in Levi's favor was not clearly erroneous.

(iii) Economic and other considerations

As a threshold matter, we disagree with the government's contention that this fourth *Mast* factor "eviscerates" the purpose of subheading 9802.00.80 due to this factor supposedly permitting improper advancements in value. Advancements in value of the assembled merchandise are, of course, only permissible to the extent that they comply with the terms of subheading 9802.00.80. However, the question posed by this factor, whether there are economic or other practical justifications for performing the assembly operation abroad, is an entirely different question to whether the merchandise at issue has been subject to an improper advance-

ment in value. Indeed, while the latter inquiry simply focuses on the value of the particular merchandise, the former looks more broadly to matters such as economic efficiency and general business strategy. Thus, we do not agree that this factor in any sense "eviscerates" the purpose of the subheading. In any event, *Mast* is binding precedent and we cannot revise it, except *in banc*.[2] *See South Corp. v. United States*, 690 F.2d 1368, 1370 n.2, 215 USPQ 657, 658 n.2 (Fed. Cir. 1982) (*in banc*).

The Court of International Trade's determination that economic and other considerations weigh in favor of granting the partial duty exemption was not clearly erroneous. Indeed, evidence was presented that certain imperfections are only apparent after the stonewashing and that it is, therefore, convenient to have the repair department of the assembly plant on site to make these corrections. Moreover, if the jeans are stonewashed elsewhere, it is apparently more difficult to identify the party to be made financially responsible for any damaged jeans. There was also evidence presented that shipping the jeans back to the United States for stonewashing can cause delays of several weeks and cause additional labor costs because the jeans have to be unpacked in the United States and then, after the stonewash, repacked, inspected, and tagged for the market in the United States. Finally, we find no merit in the government's argument that the stonewashing process cannot be considered minor because senior Levi corporate officers are involved in

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[2] Of course, "we do not read *Mast* as announcing factors that must invariably be used to the exclusion of all others, or that all such factors are pertinent in every case involving [subheading 9802.00.80]." *GM*, 976 F.2d at 719-20, 11 Fed. Cir. (T) at 4.

selecting the colors and shades desired from the stonewash. Plainly, senior management will invariably be involved in broad decision-making regarding production facilities and the product line. Not surprisingly, there is no authority or precedent for the proposition that this somehow disqualifies an importation from the partial duty exemption.

Consequently, because the Court of International Trade's determinations regarding the three disputed *Mast* factors were not clearly erroneous, we do not disturb the court's overall weighing of the factors to determine that the stonewashing process was minor and incidental to assembly.

CONCLUSION

Because the Court of International Trade's non-deferential review of Customs's interpretation and determination complied with that court's statutory mandate and applied the correct law, and because the court's determination that the stonewashing process was minor and incidental to assembly was not clearly erroneous, we

AFFIRM.

APPENDIX B

UNITED STATES COURT OF
INTERNATIONAL TRADE

Slip Op. 97-79
Court No. 93-11-00726

LEVI STRAUSS & COMPANY, PLAINTIFF

v.

THE UNITED STATES, DEFENDANT

[June 19, 1997]

OPINION

MUSGRAVE, Judge.

Plaintiff Levi Strauss & Company ("Levi") brings this action to contest the denial of a protest by the United States Customs Service ("Customs") that sought duty allowances for U.S. origin cotton denim fabric components that were shipped to Guatemala for assembly and reentered into the U.S. Levi requested that the subject merchandise be allowed partial duty allowances under subheading 9802.00.80 of the HTSUS arguing that the cotton denim components were not advanced in value or improved in condition other than by the actual assembly or by minor operations incidental to assembly. Customs denied the protest on the basis that the "enzyme-washing" process, commonly re-

ferred to as stonewashing, placed the subject merchandise out of the purview of subheading 9802.00.80 because the finishing operations were not minor or incidental to assembly. The Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1581(a) and finds that enzyme-washing in this case was incidental to assembly and orders Customs to refund the amount of duty in question with interest.

Background

The subject merchandise is 100% cotton denim fabric components manufactured in the U.S. and then exported to Guatemala for assembly into boy's cotton denim jeans known as style "550" five-pocket denim jeans. The denim fabric is cut-to-shape by Precision Cutting, Inc. in Spartanburg, S.C. and along with other components of the finished product including buttons, thread, zippers and other trim items, is transported to a Guatemalan assembler/laundry known as Koramsa, S.A. Koramsa assembled the denim jeans from the material supplied entirely by Levi. Immediately after assembly, the denim jeans were enzyme-washed, dried, pressed, labeled, inspected, sorted and packed for shipment to the U.S.

Upon importation into the U.S. in 1993, the subject merchandise was classified by Customs as boy's 100 percent cotton woven trousers under HTSUS subheading 6203.42.40 with a duty rate of 17.7% *ad valorem.* Levi timely filed a protest claiming that the cost or value of the U.S. cut-to-shape denim fabric components should have been deducted from the duty assessment under subheading 9802.00.80 of the HTSUS. Customs denied the protest on the grounds that the enzyme-washing process employed by Levi was not a minor operation incidental to the assembly process as con-

templated by subheading 9802.00.80. Levi timely filed a summons and complaint with the Court contesting Customs' protest denial.

Standard of Review

Under 28 U.S.C. § 2639(a)(1), Customs' decision is "presumed to be correct" and the "burden of proving otherwise shall rest upon the party challenging such decision."[1] However, recent decisions from the Court of Appeals for Federal Circuit ("CAFC") have ruled that the presumption of correctness applies solely to factual questions and this Court's duty is to find the correct result.[2] The Court reviews the ultimate question in a classification case *de novo*. As the Court has

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[1] 28 U.S.C. § 2639(a)(1) (1994).

[2] The duty of the Court to find the correct result in a classification case stems from both legislative and judicial sources. "[T]he trial court . . . must consider whether the government's classification is correct, both independently and in comparison with the importer's alternative. . . . [T]he court's duty is to find the correct result, by whatever procedure is best suited to the case at hand." *Jarvis Clark Co. v. United States*, 2 Fed.Cir. (T) 70, 75, 733 F.2d 873, 878 (1984). "If the Court of International Trade is unable to determine the correct decision on the basis of the evidence presented in any civil action, the court may order a retrial or rehearing for all purposes, or may order such further administrative or adjudicative procedures as the court considers necessary to enable it to reach the correct decision." 28 U.S.C. § 2643(b). *See Goodman Mfg., L.P. v. United States*, 13 Fed.Cir. (T) ——, ——, 69 F.3d 505, 508 (1995) (the statutory presumption of correctness attaches only to an agency's factual determinations) and *Rollerblade, Inc. v. United States*, 112 F.3d 481, 484 (1997) (legal issues are not afforded deference under 28 U.S.C. § 2639 or under the administrative deference standard promulgated in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984)).

found, classification decisions entail a three step process.

> The purely factual inquiry in every classification case involves determining what the subject merchandise is and what it does. The purely legal question involves determining the meaning and scope of the tariff provisions. The ultimate mixed question becomes whether the merchandise has been classified under an appropriate tariff provision, or equivalently, whether the merchandise fits within the tariff provision. This ultimate issue involves both a legal and factual component: indeed the ultimate issue is an inseparable hybrid of the discrete factual and legal inquiries and is therefore a mixed question of law and fact reviewable *de novo*.

Bausch & Lomb, Inc. v. United States, 21 CIT ——, ——, 957 F.Supp. 281, 284 (1997). The purely factual inquiry is subject to the "clearly erroneous" standard while the purely legal question and the ultimate mixed question of law and fact are reviewable *de novo*. *Id.* at 284.

Although this case comes before the Court for a review of Customs classification pursuant to 28 U.S.C. § 1581(a), the issue involved does not confront nor generate the typical classification consideration. Unlike most classification reviews, there is no contention between the parties as to competing tariff provisions: under subheading 9802.00.80 the subject merchandise either satisfies the statute or it does not. Therefore, the purely legal question found in most classification cases has already been answered. Further, the parties in the instant case have no argument as to the material facts at issue thereby precluding the need to answer the purely factual questions involved in a classification

case. What remains is the ultimate mixed question of law and fact, or whether the facts satisfy or fit the statutory standard which the Court reviews *de novo* to determine the correct result.

Discussion

Levi contests Customs' denial of a protest seeking duty allowances under HTSUS subheading 9802.00.80 for the U.S. origin cut-to-shape denim fabric components shipped to Guatemala and reentered into the U.S. Customs denied the duty allowance based on the conclusion that the enzyme-wash performed in Guatemala advanced the value or improved the condition of the U.S. origin components in a significant manner thereby placing the subject merchandise outside the scope of subheading 9802.00.80. The statute together with its legislative history and relevant case law lead the Court to find that the added value or improvement in condition provided by the enzyme-wash was minor and incidental to the assembly process qualifying the subject merchandise for duty allowance under subheading 9802.00.80.

Subheading 9802.00.80 provides that:

> Articles, except goods of heading 9802.00.90, assembled abroad in whole or in part of fabricated components, the product of the United States, which (a) were exported in condition ready for assembly without further fabrication, (b) have not lost their physical identity in such articles by change in form, shape or otherwise, and (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process such as cleaning, lubricating and painting.

> [With a general rate of duty of:]
>
> A duty upon the full value of the imported article, less the cost or value of such products of the United States . . .

HTSUS subheading 9802.00.80 (1996). In order for goods to be allowed 9802.00.80 status, all three subparts must be satisfied. In the instant case, the parties are not contesting subparts (a) and (b) of subheading 9802.00.80. The parties and the Court agree that the first section of subpart (c) is not at issue since the enzyme-wash does advance the value of the denim fabric components as well as improve their condition. This leaves a single question of whether the enzyme-wash falls into the exception of subpart (c): is the enzyme-wash an operation incidental to the assembly process?

The legislative history of HTSUS subheading 9802.00.80 is illuminating. The predecessor of subheading 9802.00.80, item 807.00 of the TSUS was amended in 1965 and the House Report states:

> The amended item 807.00 would specifically permit the U.S. component to be advanced or improved "by operations incidental to the assembly process such as cleaning, lubricating, and painting." It is common practice in assembling mechanical components to perform certain incidental operations which cannot always be provided for in advance. . . . Such operations, if of a minor nature incidental to the assembly process, whether done before, during, or after assembly, would be permitted even though they result in an advance in value of the U.S. components in the article assembled abroad.

H.R.Rep. No. 88-1728, at 46 (1964). The predecessor to the CAFC, the U.S. Court of Customs and Patent Appeals, interpreted the language of the legislative history and forged a set of criteria to determine whether a process is incidental to assembly in *United States v. Mast Industries, Inc.*, 69 C.C.P.A. 47, 668 F.2d 501 (1981). The *Mast* court found that the "legislative intent was to not preclude operations that provide an 'independent utility' or that are not essential to the assembly process; rather, Congress intended a balancing of all relevant factors to ascertain whether an operation of a 'minor nature' is incidental to the assembly process." *Id.* at 53-54, 668 F.2d at 506. The *Mast* court then listed the relevant factors useful in ascertaining whether a process is incidental to assembly:

> (1) Whether the cost of the operation relative to the cost of the affected component and the time required by the operation relative to the time required for assembly of the whole article were such that the operation may be considered "minor."
>
> (2) Whether the operations in question were necessary to the assembly process....
>
> (3) Whether the operations were so related to assembly that they were logically performed during assembly.
>
> [(4) W]hether economic or other practical considerations dictate that the operations be performed concurrently with assembly.[3] *Id.* (citations omitted).

The application of these so-called "*Mast* factors" facilitates the Court's resolution of whether the enzyme-wash employed by Levi is incidental to the assembly of the imported denim jeans.

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[3] The fourth factor was not at issue in *Mast* but the court noted its potential relevance in other actions.

I. Cost and Time Comparisons

The first *Mast* factor is composed of a cost element and a time element. In weighing these elements, courts have first been obliged to define the scope of the contested operation as well as the scope of the comparative assembly process. In a recent CAFC decision reviewing duty allowance for an intricate painting procedure, the court defined the scope of the contested operation to be comprised of the total of all of the painting steps in order that item 807.00 was not undermined "by allowing major and significant operations to be broken down to a point where each step could be called minor." *General Motors Corp. v. United States*, 16 Fed.Cir. (T) ——, ——, 976 F.2d 716, 720 (1992). Since the scope of the enzyme-wash procedure at issue here is well-defined, the danger lies in defining the scope of the comparative assembly process; limiting the scope of the comparative assembly process directly increases the importance of the operation which would allow potentially minor steps to be built up to major and significant operations.

The Court notes the subtle difference in the wording between the cost comparison and time comparison in *Mast*. The *Mast* court perspicaciously compared the "cost of the operation relative to the cost of the *affected component* " which properly measures the relative importance of the process at issue with the subject merchandise considered for the duty allowance.[4] The correct cost comparison is accordingly made between the cost of the enzyme-wash process and the cost of the denim fabric components, which is the subject of the

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[4] *United States v. Mast Industries, Inc.*, 69 C.C.P.A. 47, 54, 668 F.2d 501, 506 (1981) (emphasis added).

duty allowance at issue here. Model cost comparisons measure the percentage of relative specific costs by simply dividing the cost of the process by the component cost which yields a percentage representing that specific costs' relative importance. Applying that methodology, the relative cost is computed by dividing the enzyme-wash cost of $.80 by the denim fabric cost of $2.96 resulting in a figure of 27%.

In *General Motors*, the CAFC also compared capital investment costs in its overall cost determination. *General Motors Corp. v. United States*, 16 Fed. Cir. (T) ——, ——, 976 F.2d 716, 721. Levi uses the same capital equipment for all of its washing operations. The Court finds that the capital investment cost, therefore, is minor. Taken together, the cost of the enzyme-wash relative to the denim fabric components and the capital investment cost are minor and incidental to the assembly process. The Court finds that the cost comparison weighs in favor of granting the duty allowance for the denim fabric components at issue.

Time comparisons provide concurring results. In contrast to the cost comparison, the time comparison promulgated from the *Mast* court gauged "the time required by the operation relative to the time required for assembly of the *whole article*." *United States v. Mast Industries, Inc.*, 69 C.C.P.A. 47, 54, 668 F.2d 501, 506 (1981) (emphasis added). Levi washes 296 pairs of denim jeans in a single wash which takes 99 minutes. Customs argues that the total enzyme-wash time of 99 minutes must be used for each garment assembled. The Court disagrees with that analysis since this would allow potentially minor steps to be built up to major and significant operations. The correct wash time per garment is determined by dividing the time of the wash

by the number of garments washed. The result is that the enzyme-wash takes .334 minutes per garment. The per garment total assembly time is nineteen minutes. The relative time is calculated by dividing the per garment wash time by the per garment total assembly time which results in a 1.1% relative time. The Court finds that 1.1% represents a minor time interval and, together with the cost comparisons, is incidental to the assembly process.

II. Necessary to the Assembly Process

Although enzyme-washing is closely related to the assembly process, the process cannot be said to be necessary to the assembly process. In manufacturing other apparel, Levi sends fully assembled garments to separate enzyme-washing facilities. In fact prior to installation of the enzyme-wash machinery in Guatemala, Levi shipped the assembled denim jeans to U.S. finishing facilities where the enzyme-wash was conducted. The Court finds that the enzyme-wash procedure is not necessary to the assembly process and this factor weighs against granting the duty allowance under subheading 9802.00.80.

III. Logically Performed During Assembly

The third *Mast* factor assesses the need for the performance of the enzyme-washing operation during the assembly process. Customs argues that the enzyme-wash is "not at all directly related to the sewing operations which constitute assembly here." Def.'s Post Trial Br. at 29. This claim, however, ignores the true focus of this factor which is whether the operation in question is logically performed during the assembly process. The entire inquiry may be aptly described as determining whether there is a direct relationship between the

enzyme-wash and the whole assembly process performed overseas, but the Court finds that the aim of the third *Mast* factor is to ascertain whether the enzyme-wash is logically performed during the assembly process. Levi has asserted that the enzyme-wash is "more sensibly performed under the same roof at the assembly plant" which is "due to the nature of the process and the requirement that it be completed prior to the other finishing operations." Pl.'s Post Trial Br. at 9. The Court finds the enzyme-wash operation is logically performed at the situs of the assembly process where all other assembly and post-assembly steps are performed and where the trained personnel are located. Transferring the enzyme-wash process would entail the utilization of a separate set of production factors which the Court finds would favor the performance of the enzyme-wash at the plant in Guatemala. This *Mast* factor weighs in favor of providing duty allowance to the denim fabric under subheading 9802.00.80.

IV. Economic and Practical Considerations

Customs contends that this criterion has no bearing on the resolution of the issue before the Court. Customs states,

> both item 807.00(a) and (c) contemplate that there will be prohibitory non-assembly operations performed concurrently with assembly. Therefore, if this factor were utilized, as indicated by *Mast*, it would essentially eviscerate the clearly stated prohibited operations contemplated by item 807.00(a), and the prohibited advancements in value or improvements in condition performed before, during, or after assembly, which are implicit in item 807.00(c).

Def.'s Post Trial Br. at 29-30. Customs' interpretation of the fourth *Mast* factor is mistaken. The fourth *Mast* factor does not violate either subpart (a) or (c) of item 807.00; in fact, as stated in this opinion and agreed to by the parties, the sole question at issue is outside of the purview of subpart (a) and the first element of subpart (c), which Customs calls into question here.

Levi states that there are numerous economic and practical reasons for conducting the enzyme-wash at the situs of the assembly plant in Guatemala. Levi argues that its ability to detect and correct sewing and laundry defects would be compromised since these defects are more easily discovered after washing the garment. Pl.'s Post Trial Br. at 9. Levi also contends that performing the enzyme-wash on site in Guatemala produces more first quality garments and reduces the time it takes to get the garments to the buyer. *Id.* at 9-10. Additional labor costs would also be incurred if the enzyme-wash process were performed in the U.S. as the garments would have to be unpacked and repackaged. *Id.* at 10. The Court finds that there are economic and practical advantages of performing the enzyme-washing operation at the site of final assembly. This factor weighs in favor of granting duty allowance under subheading 9802.00.80.

V. Protection of the U.S. Industry

Customs makes a broad policy argument concerning what Customs proclaims as Levi's embarkation on a course of moving operations overseas that will negatively impact on the U.S. domestic industry. Def.'s Post Trial Br. at 2. Customs states,

> It is a basic principle of Customs jurisprudence that tariff laws were intended to raise revenues and

> were enacted to "encourag[e] the industries of the United States. ["][sic] While Levi may generally be considered a domestic company, when we are discussing the transfer of United States operations abroad the real domestic industry that is protected and must be "encouraged" by the limitations Congress placed upon the grant of duty free treatment in heading 9802 is the United States finishing industry that may be seriously injured by the transfer of finishing operations abroad, and the domestic industry that manufactures machinery and equipment in the United States that is clearly going to be injured by the transfer of finishing operations to Guatemala, which purchases archaic equipment from Korea due to Guatemala's low labor costs.

Def.'s Post Trial Br. at n. 1 (citation omitted). The Court notes that this argument is misplaced. The parties have not submitted and the Court is not aware of any evidence to substantiate the claim that the legislative intent behind subheading 9802.00.80 and its predecessor item 807.00 was to protect the domestic industry from U.S. companies' moving operations offshore. The only discussions of the intent behind the enaction of item 807.00 was to allow U.S. produced goods to compete with foreign made goods, which is exactly what Levi has done here.[5]

The argument that Customs forwards cuts both ways. By denying the duty allowance, there is a further benefit to the U.S. company to relocate their entire operation offshore. Recognizing this danger Chief

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[5] *See Free List, Special and Administrative Provisions: Hearings on the Tariff Act of 1929 Before the Committee on Finance*, 71st Cong. Vol. 6, 125-134 (1929).

Judge Nies warned that "[b]ecause of the denial of the deduction for these United States components, another part of the fabrication of automobiles in the United States will likely be lost. This cannot be the intent of Congress." *General Motors Corp. v. United States*, 16 Fed.Cir. (T) ——, ——, 976 F.2d 716, 723 (1992). What is to prevent Levi from moving the fabric manufacturing and cutting operations offshore when the denial of duty allowance increases domestic costs beyond the costs incurred overseas? The Court is reluctant to wade into these turbulent policy waters particularly when neither the statute nor its legislative history compel the Court.

VI. Other Considerations

Finally, the Court finds that the enzyme-wash is analogous to cleaning and painting which the statute specifically lists as being minor and incidental to the assembly processes. The enzyme-wash does not add anything to the denim fabric, it simply removes a measure of the indigo dye and gives the denim fabric a certain amount of abrasion that would naturally come from washing and wearing the denim jeans. Further, the enzyme-wash does not change the composition or structure of the denim fabric. Similarly, in *Haggar Apparel Co. v. United States*, 20 CIT ——, 938 F.Supp. 868 (1996), the Court found that the curing operation which imparted crease retention and seam and surface flatness to men's pants was minor and incidental to the assembly process. The enzyme-wash is directly comparable to the curing operation in *Haggar* and the Court finds that the same reasoning and conclusion are applicable to the instant case.

Taken as a whole, the *Mast* factors as applied to the instant case and all other considerations weigh in favor

of granting the duty allowances. Both cost and time comparisons are evidence that the enzyme-wash is incidental to the assembly process involved in producing the denim jeans in question. The enzyme-wash procedure is not necessary to the assembly process but it is logically, economically and practically performed in conjunction with the assembly process. Therefore, the balancing of all of the relevant factors before the Court weighs in favor of granting the duty allowance under subheading 9802.00.80 for the U.S. produced denim fabric.

Conclusion

For the foregoing reasons, the Court finds that the denim fabric is correctly classified under HTSUS subheading 9802.00.80.

JUDGMENT

Upon conducting trial, reading plaintiff's pretrial and post trial briefs, defendant's pretrial and post trial briefs, and upon consideration of all other papers and proceedings had herein, it is hereby

ORDERED that the defendant reliquidate the subject entries with a duty allowance for the value of the U.S. origin fabric components under HTSUS subheading 9802.00.80; and it is further

ORDERED that defendant refund the duties paid on the U.S. origin fabric together with the attributable costs such as cutting and inland transportation with interest.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

No. 97-1536

LEVI STRAUSS & COMPANY, PLAINTIFF-APPELLEE

v.

UNITED STATES, DEFENDANT-APPELLANT

JUDGMENT

ON APPEAL from the United States Court of International Trade
in CASE NO(S). 93-11-00726.

This CAUSE having been heard and considered, it is ORDERED AND ADJUDGED:

AFFIRMED.

ENTERED BY ORDER OF THE COURT

/s/ Illegible

DATED Sep. 22, 1998

ISSUED AS A MANDATE: DECEMBER 1, 1998

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APPENDIX D

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

[Filed: Nov. 24, 1998]

ORDER

Before: NEWMAN, Circuit Judge, SKELTON, Senior Circuit Judge, and MICHEL, Circuit Judge.

A petition for rehearing having been filed by the APPELLANT, and a response thereto having been invited by the court and filed by the APPELLEE,

UPON CONSIDERATION THEREOF, it is

ORDERED that the petition for rehearing be, and the same hereby is, DENIED.

The mandate of the court will issue on December 1, 1998.

FOR THE COURT,

/s/ JAN HORBALY
JAN HORBALY
Clerk

Dated: November 24, 1998

cc: Saul Davis
Edward M. Joffe

LEVI STRAUSS & CO V US, 97-1536
(CIT - 93-11-00726)

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Note: Pursuant to Fed. Cir. R. 47.6, this order is not citable as precedent. It is a public record.

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